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To: Mr. Giuseppe Vegas
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This letter is to notify to You a position shared by a group of academics, consumers associations, unions and other representatives of investors' interests concerning the proposals expressed in the consultation paper "*CESR's level 3 guidelines on the selection and presentation of performance scenarios in the Key Investor Information document (KII) for structured UCITS*", published last 20 July 2010, as a part of the implementation process (level 3 guidelines) of the revised UCITS Directive (2009/65/EU).

The above mentioned group - whose views are quite similar to those submitted by several participants to the consultation process - wants to express disappointment for the choice made by the CESR to implement the *performance scenarios* of article 78, par. 3 (c) of the level 1 UCITS Directive according to a *what-if* solution instead that by means of the so-called *probabilistic table*.

Since we are conscious that transparency is the main topic of this century, particularly with respect to retail investors, we see this choice is a significant and unexpected backward step. It is in fact the main goal of regulation to provide retail investors with adequate information on the key characteristics of financial products and the associated risks and costs so that they can be effectively supported in the

selection of solutions that best suit their needs. This selection cannot avoid a probability judgement from any individual, and each of them, independently from her education, country and social condition would always ask the same question: **what are the risks** I am going to bear with this investment, with respect to a safer one? The probabilistic table provides a direct answer to this question, and answering this question must be mandatory for any financial institution proposing an investment.

The choice of dismissing the *probability table* as mandatory disclosure is an unforgiveable setback for the following reasons:

- 1) **what-if is a marketing tool and it is not a transparency tool:** what-if analysis is based on a particular evolution of the market and as such it is completely arbitrary, and subject to manipulation and distortion. As such, it may be an important marketing tool, but cannot be confused with transparency;
- 2) **scenarios can only be stated in terms of probability:** transparency has to do with helping retailers to make clear the probability of success of their investments, while a *what-if* scenario provides a representation of a single state of the world out of an infinity of other possible ones, and as such has zero probability; collecting all scenarios and distinguishing among good, bad and fair necessarily leads to the probability table. Without this additional piece of information on probabilities the *what-if* would only favour investors' confusion and misunderstanding since their natural interpretation would be to consider each of the three outlined *what-if* scenarios as exhausting all possibilities and having the same probability, which is clearly false;
- 3) **comparison of different products can only be done in terms of probability:** in a *what-if* disclosure, every product is evaluated (and not measured) in a different scenario and cannot be compared across different asset classes and products unless all possible scenarios are collected (and measured) in a *probability table*;
- 4) **probabilistic comparison across products must rely on a common reference, the safest financial investment:** the probabilistic table provides a representation focused on four main performance scenarios (negative return and positive return respectively below, in line and above the risk-free asset) each one identified by the associated probability and by a value which synthesizes the returns achievable in that scenario. In this way investors get a fair comprehension of the performances attainable by the product, both in terms of capital preservation and of chances of earning more than from the riskless asset;
- 5) **financial products are designed using probability:** any asset manager and structurer address the same basic question as retail investors do: how much am I likely to perform better than other products? Differently from retail investors, they must be endowed with technical tools and skills to provide an answer. So, *disclosing* this information must be mandatory from a regulatory point of view because *having* this information is mandatory from a deontological point of view. Moreover, given the in-house availability of the said tools and skills, issuers can provide consumers with this key information without any additional burden with respect to their usual pricing and risk management activities.

Given these arguments, which are grounded on the basic principles of finance, we ask:

- 1) Why was the *what-if* approach presented in the consultation document as the only viable solution to implement level 1 provisions?
- 2) Is the dismissal of the probability table as mandatory disclosure in favour of the *what-if* approach consistent with the preferences of retail investors? We are aware of studies requested by the European Commission on the effectiveness of different forms of disclosure to consumers. How do the results of these studies fit with the proposal made in the consultation paper?
- 3) Where and when were the arguments in favour of the *probability table* expressed by the respondents to past consultations on the KII contrasted? Why have they only been dismissed with no argument?

If any decision will be taken without answering these questions we are afraid we will have to conclude that the struggle for transparency will remain on the exclusive domain of academics and consumers' associations. We want to be confident that this will not be the outcome. Therefore, on behalf of investors' protection, we believe that it is necessary, as suggested by some participants to the consultation process, to start with **a new consumer test** focused on the effectiveness of the *probabilistic table* approach versus the *what-if scenarios*.

Moreover, it is our opinion that the final guidelines which will be published by the CESR in this matter should not be allowed to weaken the level of investors' safeguard which has been reached by the virtuous solutions based on probabilistic approaches adopted by some member countries, including Italy.

In this perspective, if at the European level there would remain a huge discrepancy among the several regulators and stake-holders about what approach should be pursued, we firmly believe that, in the light of the prior task of investors' protection, the better solution should be to endow each competent authority with the power to apply its disclosure regime on performance scenarios to all structured Ucits marketed inside its borders irrespective of the country where these products are issued.

Indeed, even if this solution could appear a violation of the maximum harmonization principle, nobody could disregard that the blind pursuit of this latter principle at the cost of a weakened investors' safeguard would be fully equivalent to miss the opportunity of achieving a Pareto optimum, which, by definition, will improve the position of some consumers without additional damages for the others.

We would appreciate your immediate attention on this matter.

Best regards.

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